



STATE BOARD OF EQUALIZATION STAFF LEGISLATIVE BILL ANALYSIS

Date Introduced	2/25/00	Bill No:	AB 2652
Tax:	Property	Author:	Pescetti
Board Position:	Support, if amended	Related Bills:	

BILL SUMMARY:

This bill would require the Board to conduct annual studies to obtain data needed to update replacement cost factors and useful life tables.

ANALYSIS:

Current Law:

Section 401.5 of the Revenue and Taxation Code requires that the Board shall issue to assessors data relating to the costs of property and other information that will promote uniformity in appraisal practices and in assessed values throughout the state.

The Board complies with Section 401.5 by issuing various Assessors' Handbooks and Letters to Assessors (LTA). The Board specifically complies with Section 401.5, for business property by annually publishing Assessors' Handbook Section 581, *Equipment Index and Percent Good Factors*. This handbook contains several tables of equipment index factors and percent good factors.

Additionally, Section 15606 of the Government Code, subdivision (e), requires the Board to "[p]repare and issue instruction to assessors designed to promote uniformity throughout the state and its local taxing jurisdictions in the assessment of property for the purposes of taxation." Section 15606 concludes by stating that "[t]his section is mandatory."

Proposed Law:

This measure would statutorily require the Board of Equalization to annually conduct a study to obtain those data that are necessary to update replacement cost factors and useful life tables used in determining the assessed value of taxable business equipment and other taxable business property.

The primary method to value tangible personal property is the Replacement Cost New Less Depreciation (RCNLD) approach. The two primary variables in the calculation of an accurate RCNLD indicator are the replacement cost factors and the economic life of the property.

This staff analysis is provided to address various administrative, cost, revenue and policy issues; it is not to be construed to reflect or suggest the Board's formal position.

In General:**Locally Assessed Property**

For locally assessed property, the RCNLD indicator is the widely used method of valuing fixtures and personal property. Many of the current replacement cost factors and life tables that the staff of the Property Taxes Department use when reviewing the assessments of county assessors were initially developed in the 1970's. Some of these life tables were revisited again in 1982 by BOE staff. Therefore, the life tables that are available are dated and do not include tables for some of the newer, high-technology industries. The replacement cost factors have been updated periodically, but need restructuring to reflect newer industries and changing technology. A substantial number of tax appeals at both the state and local level originate due to disagreement over appropriate factors and lives. This litigation presents a risk for local governments which seek a more predictable tax base to address increasing demands for services.

As part of the BOE's oversight of county assessors' jurisdictions, the BOE's County Property Tax Division samples the assessment of personal property and fixtures when reviewing county assessment programs. Personal property is defined in the statutes as all property except real estate. Fixtures are defined in the statutes as items of tangible property, the nature of which was originally personal property, but which are classified as realty for property tax purposes because it is physically attached or, in terms of construction, annexed to realty with the intent that it remain annexed indefinitely. The assessment of personal property, for property tax purposes, is based on the fair market value of the property on each lien date (every January 1).

To determine the fair market value of fixtures and personal property, counties most often use RCNLD. When sampling, BOE staff generally uses the RCNLD to determine the fair market value of fixtures and personal property. The critical problem is that the estimated economic lives established in the current policy (formerly known as Policy and Procedures No. 10) are decades old and do not address current high-technology related industries. This policy, dating back to the 1970's, contains the estimated economic lives for the fixtures and personal property assessed in the state. There are 35 industry groups included in the current policy.

The primary purpose of publishing guidelines for county assessors is to facilitate uniformity of assessments in the state. The question of what is the proper economic life to be used, however, is often the basis of appeal by property owners who may dispute their assessed values. A review of appeals of locally assessed industrial property, involving fixtures and personal property, indicates that approximately 17,000 appeals were filed in 1995-96 (which is the most recent year for which data are available). Many of these appeals are based on a claim that obsolescence was not recognized or allowed or that the replacement cost factors and economic lives used were not current or realistic.

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State-Assessed Property

Pursuant to Article XIII, Section 19, of the California Constitution, the State Board of Equalization is required to annually assess property (except franchises), owned or used by regulated railway, telegraph, or telephone companies, car companies operating on railways in the state, and companies transmitting or selling gas or electricity. The State Constitution also requires the Board to annually assess pipelines, flumes, canals, ditches or aqueducts lying within two or more counties. Except for private car companies, the assessed values of these public utility properties are allocated to the counties based on property location. Properties assessed by the Board are not subject to the provisions of Proposition 13, and accordingly are assessed annually at fair market value.

Background:

Recognizing the importance of having updated data, the *1999-2000 Governor's Budget Summary*, (page 176), included the following statement: "To ensure that statewide property tax assessment standards for tangible assets in California are both fair to the business community and provide stable tax bases for local jurisdictions, the Administration will continue to examine the potential impact of updated replacement cost factors used in the valuation of state and locally assessed property, and may review any funding needed for updating factors in the spring of 1999."

In the spring of 1999, the Board of Equalization requested additional funds beginning in Fiscal Year 1999-2000 and each of the next four fiscal years to contract with a consultant to assist existing staff in developing fourteen replacement cost factor and economic life studies over a five-year period. The studies would assist in valuing tangible assets for state-assessed and local property tax.

The 1999-2000 Budget Act included \$250,000 for the Board to conduct *preliminary* assessment studies. The Budget Act control language specifies that each preliminary assessment is to (1) include an estimate of the potential range of impact on state and local revenues from adoption of new replacement cost factors and useful life tables, (2) discuss the frequency with which the factors and tables should be updated to remain reasonably accurate, and (3) provide an analysis of any methodological issues which may be faced in designing data collection and analysis methods for each study. The language requires the Board to present the results of the preliminary assessment studies to Legislative Committees that consider taxation measures.

The Board of Equalization issued a Request for Proposal (RFP) seeking consultant services to assist in conducting this preliminary assessment study in September of 1999. Copies of the RFP were released to 42 prospective bidders; however, no proposals for the project were ultimately submitted.

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COMMENTS:

1. **Sponsor and purpose.** The measure is sponsored by the author to statutorily specify that the Board of Equalization undertake these studies.
2. **These studies may result in the ability to calculate more reliable assessed values.** Studies may produce more accurate assessments of fixtures and personal property on both state and locally assessed property and could avoid costly lawsuits provided that both assessors and industry felt confident in the results of these studies. Accordingly, updating this information could result in fewer disputes over values and consequently, a decrease in appeals filed. The cost avoidance for both private industry and government in resolving appeals could be substantial. Furthermore, the studies could assist in ensuring a more predictable tax base for local governments.
3. **There has been some concern about the impact the studies may have on affected businesses and property tax revenues.** The purpose of the studies the Board wanted to undertake with the assistance of technical experts was to provide *objective* and *defensible* replacement cost factors and economic life tables that promote statewide uniformity. The validity of the current recommended lives and tables is increasingly questioned.
4. **There is no requirement that county assessors must use the data developed by the Board.** In January 2000, the California Assessors' Association issued a document entitled "Business Assessment Factors." This document provided several tables of equipment index, percent good, and valuation factors for use by all California Assessors in mass appraisal programs. The document incorporated many tables from the Boards Assessors' Handbook Section 581, *Equipment Index and Percent Good Factors* with the notation that it must be used in conjunction with the Board's document.
5. **The Board recently conducted studies in the Computer and Bio-pharmaceutical industries.** Obtaining the raw data needed to complete these studies from industry proved difficult. It may be helpful to require that industries participate in these studies with the assurance of complete confidentiality of the data supplied.
6. **This bill requires that the Board "annually" conduct a study.** It would not be possible to conduct studies every year in all industry areas. The Board could, with proper funding, undertake sequential studies in various subject areas each year. The Board has previously noted a need for studies in order of priority for the following areas for property assessed by local county assessors: Aerospace Industry, Computer Manufacturing, Semi-Conductor Manufacturing, Petroleum Refining, Chemical and Allied Products, and Electronic Assembly. For property assessed by the Board of Equalization: Local Exchange, Interchange, Wireless, Nuclear Generation, Fossil Fuel Generation, Hydro-Electric, Natural Gas

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Distribution, Natural Gas Transmission, and Natural Gas Storage Reservoirs. The following language is suggested for clarification:

407.5. The State Board of Equalization shall annually conduct a study to obtain those data that are necessary to update replacement cost factors and useful life tables used in determining the assessed value of taxable business equipment and other taxable business property. The type of property or industry selected for study each year shall be determined by the Board.

COST ESTIMATE:

A detailed cost estimate for additional staffing to perform annual studies is pending.

REVENUE ESTIMATE:

This measure has no direct revenue impact.

Analysis prepared by:	Rose Marie Kinnee	445-6777	3/27/00
Contact:	Margaret S. Shedd	322-2376	
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